In the Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-504

WILLARD BARRY AND HARRIET BARRY, PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

Petitioners challenge the decision below affirming the district court's finding that an antiquated building inherited by petitioner Harriet Barry ("Harriet") had no fair market value on the relevant valuation date, so that petitioners had no basis in the building with respect to which they could properly claim deductions either for depreciation or for the loss allegedly sustained by them upon demolition of the structure (Pet. App. A-1 to A-13, A-15 to A-27).

Petitioners are husband and wife. In 1959, Harriet inherited a parcel of valuable commercial property located in the downtown center of Colorado Springs, Colorado, the agreed value of which was $160,000. On the land was an antiquated stone and masonry building, which had been constructed prior to the turn of the century (Pet. App. A-3, A-15 to A-19). By the time Harriet inherited

the property, the building no longer had any forseeable economic potential as a commercial structure, and, moreover, had become a detriment to the overall value of the property (Pet. App. A-6, A-10, A-23, A-25). Various local building code violations precluded use of the upper two floors, and the general condition of the building made it economically unfeasible to remodel or rehabilitate the structure for commercial purposes (Pet. App. A-6 to A-7, A-19).

The property was previously owned by Harriet's mother, who, prior to her death in 1959, had entered into a lease agreement with a local bank, granting the bank a five-year lease of the property (commencing January 1, 1955) at a rental of $1,000 per month and an annual payment of $1,000 toward the real property taxes. Under the agreement, the bank at its option, could renew the lease for an additional five-year period, and was also authorized to demolish the building on the property at any time during the period of the leasehold without payment or compensation to the lessor. Those provisions comported with the bank's ultimate reason for acquiring the lease, which was to demolish the existing structure and utilize the underlying land for a parking lot and drive-in teller facility.

In the interim, the bank on two separate occasions subleased the property on a temporary basis in order to recoup its own rental expense. The lease was in effect at the time Harriet inherited the property from her mother. Shortly thereafter, the bank demolished the building (Pet. App. A-8, A-19 to A-20).

On their amended tax returns for 1959 and 1960, petitioners allocated a $45,000 basis to the building on the Colorado Springs property, and claimed depreciation deductions on the building. In 1960, they also claimed a

loss deduction for what they contended was their undepreciated basis in the building at the time of its demolition by the bank under the lease agreement (Pet. App. A-15 to A-16, A-21).

On audit, the Commissioner of Internal Revenue determined that the building had no separate fair market value and, accordingly, denied the depreciation and loss deductions. In a refund suit brought by petitioners, the district court found that the agreed value of the Colorado Springs property was solely attributable to the land and its advantageous commercial location, and that the antiquated building had no ascertainable fair market value on the relevant valuation date (Pet. App. A-1 to A-13). Noting the factual nature of the question of the building's valuation, the court of appeals affirmed (Pet. App. A-17 to A-27).

1. Sections 167(g) and 165(b) of the Internal Revenue Code of 1954, respectively, limit depreciation and loss deductions to a taxpayer's "adjusted basis" in his property, as that term is defined in Section 1011 of the Code. Section 1011, in turn, provides that the adjusted basis of inherited property is to be determined with reference to Section 1014, which states that a taxpayer's basis in property acquired from a decedent is the "fair market value of the property" on the date of the decedent's death or (as is the case here) on the alternate valuation date. "Fair market value" is defined as the price at which property would change hands between a willing buyer and a willing seller, neither being under any compulsion and both having knowledge of the relevant facts. *United States* v. *Miller*, 317 U.S. 369, 374; *In re Williams' Estate*, 256 F. 2d 217, 218 (C.A. 9).

The burden of proof was on petitioners to establish the $45,000 value claimed on their returns. *Burnet* v. *Houston*, 283 U.S. 223, 228-229; *O'Neill* v. *Commissioner*,

271 F. 2d 44, 50 (C.A. 9). At trial, the opposing parties presented expert testimony and other evidence, much of which was conflicting as to the value of the building. Finding that all of the fair market value of the realty inhered in the land and that the building was valueless, the district court resolved this factual question in favor of the government.

Petitioners argue (Pet. 7-8) that the court of appeals improperly applied the clearly erroneous rule of *Commissioner* v. *Duberstein*, 363 U.S. 278, on the ground that this case involves disputed facts while *Duberstein* did not. But the clearly erroneous rule applies whether an issue involves the resolution of disputed factual inferences as in *Duberstein*, or conflicting testimony and evidence as in *United States* v. *Yellow Cab Co.*, 338 U.S. 338, and *Zenith Corp.* v. *Hazeltine*, 395 U.S. 100, 121-123.

At all events, the district court's finding that the building had no fair market value is supported by the evidence, which included a detailed analysis by an expert witness as well as other evidence demonstrating that the building in question no longer had any economic value[1] (Pet. App. A-10 to A-12, A-23 to A-26). On the evi-

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[1]Petitioners' various allegations (Pet. 12-16) that evidence was "improperly received" or "improperly rejected" are somewhat inaccurate. They did not assert in the court below that any evidence was erroneously received or excluded (Pet. App. A-26), and their point seems to focus merely on the relative weight which the district court accorded the testimony and other evidence presented.

Moreover, petitioners' objection (Pet. 16) to the "Levy Affidavit" is unfounded. In that affidavit, an officer of one of the former sub-lessees of the property testified that the building itself was beyond rehabilitation and that the company's sole interest in the property was its valuable commercial location. While the district court initially considered the affidavit and certain of petitioners' own evidence to be technically inadmissible, the affidavit was ultimately admitted pursuant to a stipulation agreed to by petitioners

dence presented, the district court correctly concluded that the building was a detriment to the overall market value of the property, and detracted from what would have been the fair market value of the land alone had the land been independently committed to its best and highest use (Pet. App. A-10 to A-11, A-23). While petitioners introduced certain evidence indicating that the building had a standard formula value for local property tax purposes, that evidence had little relevance to the central question of the actual "fair market value" of the building.

2. Petitioners further argue for the first time (Pet. 17-18) that the controlling issue is not the fair market value of the building, but rather the proper "determination of the proportionate share of this total value to assign to the building * * *." But even apart from their failure to press this contention below, the proposed distinction is fundamentally unsound. It is impossible to allocate fair market value between land and a building thereon without determining the fair market value of each of the component properties.[2]

Finally, contrary to petitioner's contention (Pet. 20), the decision below does not conflict with *Feldman* v.

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during the district court proceedings. (See Appendix, *infra*, pp. 1a-4a.) Once the affidavit was admitted pursuant to the stipulation, it was proper for the district court to afford the testimony therein "its natural probative effect as if it were in law admissible." *E.g., Diaz* v. *United States*, 223 U.S. 442, 450-452; *Isaac* v. *United States*, 431 F. 2d 11, 15 (C.A. 9).

[2]In the usual case, the total of the fair market value of the component properties will approximate the fair market value of the entire property. This was true in this case, except that here the fair market value of the land exceeded the fair market value of the land and the building combined because the building was a detriment to the value of the entire property.

Wood, 335 F. 2d 264 (C.A. 9), or *Hightower* v. *United States*, 463 F. 2d 182 (C.A. 5). Each of those cases involved the question whether loss deductions were allowable where the taxpayer had an established undepreciated basis in property which was subsequently demolished under the terms of a lease. Since the building in this case had no fair market value on the relevant valuation date, Harriet acquired no separate basis in the building and consequently suffered no economic loss when the building was demolished.

As the court of appeals noted (Pet. App. A-27, n. 8), any conflict between *Feldman* and *Hightower*, on the one hand, and *Landerman* v. *Commissioner*, 454 F. 2d 338 (C.A. 7), and *Foltz* v. *United States*, 458 F. 2d 600 (C.A. 8), on the other, over whether a demolition loss deduction is allowable when a lease grants the lessee the option to demolish the building but does not mandate demolition, is immaterial to this case, where Harriet was found to have a zero basis in the building.

For the foregoing reasons, it is respectfully submitted that the petition for a writ of certiorari should be denied.

ROBERT H. BORK,
Solicitor General.

JANUARY 1975.

APPENDIX

(Transcript of proceedings before district court, January 26, 1973)

[369]

(Thereupon Plaintiffs' Exhibit MM was marked for identification by the Clerk.)

MR. ROSS: Your Honor, if Mr. Barry has no objection to the introduction of that affidavit, we would forego the objection to the lease.

MR. BARRY: Well, it would be difficult. It is 1972—we made all the efforts we could to rent the building, and to come in 1972 without the affidavit, without any notice, to take his deposition—we certainly think it is admissible.

Will you mark this as one group?

Judge, may we proffer all this correspondence?

THE COURT: Well, it is evident, as I look over the documents handed to me, frankly, JJ, which purports to be a proposed short-term agreement, and MM, which purports to be a 20-year proposed lease, each being documents in which the parties are Louie N. Mullin and Fashion Bar, Incorporated; that these leases—did you come into—neither the lease nor the agreement was executed.

[370]

It would seem to me that since apparently the party is still alive who has knowledge as the other party to this transaction, Mr. Jack H. Levy, that I not receive these documents into evidence in the absence of—certainly they will only have relevance as conceivably bearing on the economic value of this property; and more specifically, as it might bear on the economic value of the structure; therefore, I do not believe that I should receive them in evidence, since they were not actually executed, and the reasons for which they were not executed would become important, and in the absence of having testimony on both sides, I would not feel it would be proper to receive the testimony of Mr. Barry.

The Government apparently is willing to receive these exhibits into evidence, provided you are willing to agree to the receipt in evidence of the affidavit of Mr. Levy.

MR. BARRY: Judge—all right.

THE COURT: I make no indication other than to indicate what Mr. Ross has just said. If the parties want to stipulate this, that is up to the parties.

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MR. ROSS: May I be heard briefly? I am ready to withdraw any objections and put in Defendant's Exhibit 11 with the rest of these documents.

THE COURT: You are prepared to stipulate the receipt of all the letters?

MR. ROSS: —of the Fashion Bar, in return for our getting in the affidavit of Mr. Levy.

THE COURT: You are prepared to agree?

MR. BARRY: Oh, yes, sir.

THE COURT: Very well.

Under those circumstances, the proposed agreement, the proposed lease—

MR. BARRY: There are two leases. There were two proposed leases for the Fashion Bar.

THE COURT: JJ and MM was a short-term, and the other is a long-term?

MR. BARRY: Yes. They were both prepared by Mr. Miller.

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THE COURT: One is JJ and one is MM, so let's —so it is stipulated then that the exhibits, which I will ask Mr. Melle to read off, that relate to the Fashion Bar, the proposed transaction, may be received in evidence, together with Government's Exhibit 11—is it?

MR. ROSS: Yes.

THE COURT: —which is the affidavit of Jack Levy, who apparently is the owner of the Fashion Bar?

MR. BARRY: Yes.

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